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**A lawsuit in the making — the EPLI insurance application**

By Jackie Taylor | June 19, 2006

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Every day, the Equal Employment Opportunity Commission receives some 200 new employment practices liability complaints alleging discrimination based on race, sex, national origin, religion, retaliation, age and disability. Even if an employment-related claim is baseless, defense costs can be significant. Employment practices liability insurance (EPLI) policies can provide protection against the typical discrimination and sexual harassment suits that come to mind, as well as cover breach of employment contract and, increasingly, whistleblower retaliatory measures, libel and slander.

**Choose the right application**  
This article is meant to alert agents, broker, corporate counsel and risk managers to one potential pitfall of EPLI coverage: the insurance application. Many application questions, particularly with regard to claims issues, can be difficult, if not impossible, to answer. If the policyholder does not answer the questions on its insurance application fully, the insurance company may later say that the policyholder failed to disclose material information on the application. That may provide the insurance company with a defense to coverage. Brokers and agents often are asked by the policyholder for assistance in the completion of an application. In fact, it is not uncommon for the broker/agent to complete the application. As such, a mistake on the application can result in more than just a headache for the broker/agent — it can lead to a lawsuit.

Two EPLI applications show the range of application styles. One particularly troubling application asks if the policyholder’s officers, directors, managers or supervisory employees are aware of any “facts, circumstances, disagreements or incidents which might result in a claim” by any employee or applicant for employment, for inappropriate employment conduct, harassment or discrimination, or by any third party for harassment or discrimination. There are two problems with a question like this: First, employment issues come up every day, and it is often impossible to know what “circumstances,” “disagreements” or “incidents” may ultimately lead to a claim. Second, since a “supervisory employee” may be the culprit, he/she is often unlikely to disclose an incident to a risk manager or other company employee who is completing the EPLI application.

In contrast, a second insurance company’s application simply asks for details of all wrongful termination, discrimination, and sexual harassment claims in the prior three years and asks for details on all inquiries, investigations, grievance filings, or other administrative hearings previously filed during the last three years. For questions such as these, the applicant knows what the insurance company is asking.

**Application ‘answers’ do count**  
An insurance policy may be rescinded for misrepresentation if the insurance company can establish that a representation was false, the policyholder knew the representation was false when made or made it in bad faith, and the representation was material to the risk’s being insured.

Insurance companies are quick to argue rescission or fraud for failing to disclose, for not fully disclosing, or for putting the wrong information in an application. In one such case, the insurance company alleged that the policyholder fraudulently failed to disclose terminations of three employees before the policy was sold. Specifically, the policyholder did not disclose on a renewal application that it had terminated three employees of a subsidiary bank that it had recently acquired. Ultimately, the court held in favor of the policyholder, that is, against rescission. First, the application made it clear that the policyholder was not seeking coverage for the subsidiary’s employees. Only later did the policyholder request to add the subsidiary to the EPLI policy.

In another case, the insurance company argued that the policyholder failed to disclose claims against it when it applied for a renewal of its EPLI policy. The court held in favor of the insurance company, awarding rescission and reimbursement for amounts it paid under the policy, plus prejudgment interest. At issue was the policyholder’s failure to disclose on the renewal policy application two administrative charges for discrimination that it became aware of during the original policy period. The policyholder received copies of the charges prior to renewal, but it did not disclose the charges on the renewal application. The court granted rescission on the basis that the renewal application required disclosure of the two administrative charges.

**Avoid the loopholes**  
Do not give an insurance company a reason to deny coverage for a claim based upon an answer to a poorly worded application. If the question in the application is ambiguous or would require questioning virtually every company employee, you may need to change the question on the application itself. One other alternative is to find an EPLI application that has acceptable questions and use that application with each insurance company. The bottom line is that, post-claim, insurance companies increasingly scrutinize applications to look for a reason to rescind — do not give them an opening to argue rescission.